# The CANADA PENSION PLAN

## Financing the Canada Pension Plan

*The Canada Pension Plan (CPP) is funded from contributions made by employers, employees and the self-employed and from interest earned by investments of excess revenue. Effective January 1, 1987, changes to the financing of the Fund will ensure its continued long-term financial health.*



### The Changes

The changes are needed because:

- Canada's population is aging and will continue to do so for the foreseeable future
- benefits have been improved on several occasions since the Plan was established, with no corresponding increase in contributions
- maturing of the Plan will mean that more pensioners will be drawing benefits in the future than in the past.

The changes agreed to by the federal and provincial governments:

- a 25-year schedule of contribution rates has been established in the legislation
- the Plan will have as a target a fund equal to two years of benefits in the long term
- federal and provincial Ministers of Finance will review the 25-year schedule every five years (or earlier if benefits are changed) to ensure that the contribution rates remain appropriate and to extend the schedule for five years. The first five years of each 25-year schedule will remain set to provide certainty for business and workers
- the new schedule will come into effect January 1, 1987.

### The Contribution Rate Schedule

- contributions to the CPP are required on earnings between the Year's Basic Exemption ($2,500 in 1987) and the Year's Maximum Pensionable Earnings ($25,900 in 1987)
- when introduced in 1966, the contribution rate was deliberately set at a low rate to avoid the build-up of an excessively large fund. It was fully realized that the contribution rate would have to be increased when the Plan matured
- the combined employer/employee contribution rate will rise by 0.2 percentage points per year from 3.6% in 1986 until 1991 when it will reach 4.6%
- the contribution rate will then increase by 0.15 percentage points per year between 1992 and 2011, reaching 7.6% in 2011
- the combined employee/employer contribution rate will be 3.8% in 1987. This change will increase the annual maximum employee contribution by $23.40 in 1987. However, CPP contributions are deductible for income tax purposes. Workers earning the average wage, will therefore have their take home pay reduced by $16.00 per year in 1987.

### The Schedule of Contribution Rates

| Year | Rate* (%) | Year | Rate* (%) | Year | Rate* (%) | Year | Rate* (%) | Year | Rate* (%) |
|---|---|---|---|---|---|---|---|---|---|
| 1987 | 3.80 | 1992 | 4.75 | 1997 | 5.50 | 2002 | 6.25 | 2007 | 7.00 |
| 1988 | 4.00 | 1993 | 4.90 | 1998 | 5.65 | 2003 | 6.40 | 2008 | 7.15 |
| [illegible] | [illegible] | 1994 | 5.05 | 1999 | 5.80 | 2004 | 6.55 | 2009 | 7.30 |
| [illegible] | [illegible] | 1995 | 5.20 | 2000 | 5.95 | 2005 | 6.70 | 2010 | 7.45 |
| [illegible] | [illegible] | 1996 | 5.35 | 2001 | 6.10 | 2006 | 6.85 | 2011 | 7.60 |

...ncreases in CPP contributions for workers earning average wages* during the first ten ...ew schedule:



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Example of increases in CPP contributions for workers earning average wages* during the first ten years of the new schedule:

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| | New Contribution Rate | Total Maximum Yearly Contributions* Under Old Arrangements | Total Maximum Yearly Contributions* After New Arrangements | Amount of Annual Increase in Contributions |
|---|---|---|---|---|
| | (%) | (dollars) | | |
| 1987 | 3.8 | 421.20 | 444.60 | 23.40 |
| 1988 | 4.0 | 437.40 | 486.00 | 48.60 |
| 1989 | 4.2 | 453.60 | 529.20 | 75.60 |
| 1990 | 4.4 | 471.60 | 576.40 | 104.80 |
| 1991 | 4.6 | 489.60 | 625.60 | 136.00 |

*Assumes a 4% annual increase in average wages after 1987.

## Keeping the CPP Financially Healthy

- the federal and provincial governments have also ensured that the CPP will remain financially healthy by instituting an automatic review of the rate schedule
- this review will be conducted every 5 years and will examine the experience of the Plan with a view to keeping a minimum contingency fund equal to 2 years' benefits
- during the 25-year schedule, interest payments from the CPP Fund's investments in provincial securities will continue to help finance the benefit payments and to maintain an adequate reserve
- the governments have agreed that a reserve of 2 years' benefits is sufficiently large to cushion the effects of economic and demographic fluctuations, without building up an unnecessarily large and costly fund
- the new provisions assure that the CPP will always be able to pay the benefits promised to Canadians without requiring sudden, sharp increases in contribution rates. It puts to rest, once and for all, concerns about the Plan "going broke" and leaving Canadians without a pension.

## More Information

**A more detailed explanation of the long-term forecasts of CPP revenues and expenses can be found in the CPP Actuarial Reports, tabled in the House of Commons. The latest report was tabled on October 3, 1986.**

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